



## **STATE OF NEW JERSEY**

### ***Board of Public Utilities***

***Two Gateway Center***

***Newark, NJ 07102***

***www.bpu.state.nj.us***

### **CABLE TELEVISION**

IN THE MATTER OF THE FILING BY TWFRANCH – )	ORDER ADOPTING
ONE CO., d/b/a TIME WARNER CABLE (BERGEN )	INITIAL DECISION
SYSTEM) RATE CHANGE UNDER FCC FORM 1240 )	
UPDATING MAXIMUM PERMITTED RATES FOR )	
REGULATED CABLE SERVICES )	BPU DOCKET NO. CR02100722
)	OAL DOCKET NO. CTV9774-02N
IN THE MATTER OF THE FILING BY TWFRANCH – )	
ONE CO., d/b/a TIME WARNER CABLE (BERGEN )	
SYSTEM) RATE CHANGE UNDER AGGREGATE )	
FCC FORM 1205 DETERMINING REGULATED )	BPU DOCKET NO. CR02100723
EQUIPMENT AND INSTALLATION COSTS )	OAL DOCKET NO. CTV9775-02N

### **SERVICE LIST ATTACHED**

BY THE BOARD:<sup>1</sup>

The New Jersey Board of Public Utilities (Board) and its Office of Cable Television (OCTV), pursuant to N.J.S.A. 48:5A-1 et seq., have been granted general supervision and regulation of and jurisdiction and control over all cable television systems which operate within the State of New Jersey, subject only to the limitations of federal law. Pursuant to this authority, the within matter was opened to the Board upon the filing by TWFranch-One d/b/a Time Warner Cable, Bergen System (Time Warner), on October 1, 2002, of its FCC Form 1240 covering its Bergen New Jersey system and an Aggregate FCC Form 1205 covering all Time Warner systems nationwide, including its Bergen New Jersey system. On October 31, 2002, the Board transmitted the filing to the Office of Administrative Law (OAL) as a contested matter pursuant to N.J.S.A. 52:14B-2(b). Plenary hearings on these filings were held before Administrative Law Judge (ALJ) William Gural on May 8 and 9, 2003. Appearing in the proceeding were the Board's Staff (Staff), the New Jersey Division of the Ratepayer Advocate (RPA) and Time Warner. On July 8, 2003, Judge Gural issued his Initial Decision. On July 14, 2003, the Board received the Initial decision. On or about July 28, 2003, Time Warner and RPA filed Exceptions to the Initial Decision, with Reply Exceptions filed on August 4, 2003.

### **DISCUSSION**

The Board is the local franchising authority in New Jersey and is certified to regulate basic service rates and associated equipment and installation charges pursuant to 47 C.F.R. § 76.910. Additionally, Time Warner has the burden of proof in demonstrating the reasonableness of existing and proposed rates for basic service, associated equipment and installation charges.

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<sup>1</sup> Commissioner Jack Alter did not participate in the deliberation or the vote on this matter.

47 C.F.R. § 76.937(a). The major issue before ALJ Gural was whether Time Warner provided sufficient proof to support its request for the rate changes and increases being sought. The Board, after careful review of the record, including the Initial Decision and the Exceptions and Reply Exceptions, makes the following determinations:

#### FCC FORM 1240

FCC Form 1240 is used by a cable operator to allow for annual adjustments to regulated cable rates, and the purpose behind the form is to provide the franchising authority with sufficient background to determine if the proposed rates are reasonable as defined by the FCC. 47 C.F.R. § 76.922. In the current contested matter, the primary issue is the reasonableness of external programming costs, particularly those attributable to programming provided by the Time Warner affiliate, New York 1 News (NY1).

ALJ Gural, in his Initial Decision, determined that, in reference to the determination of the proper cost of the NY1 channel, because the channel is owned by an affiliate, and not widely distributed to non-affiliate cable providers, in-depth rate-making cost-of-service scrutiny is warranted under FCC rules. Additionally, ALJ Gural found that ledger entries presented into evidence by Time Warner did not provide sufficient detail to satisfy a cost of service review under FCC rules. The ledger entries did not contain the necessary underlying financial components needed for the Board to determine the functional financial make-up of the proposed charge, as required under the FCC's rules. Likewise, ALJ Gural found that Time Warner failed to meet its burden of proof in supporting its FCC Form 1240 filing. Accordingly, ALJ Gural determined that the 1240 rates proposed by Time Warner should be denied and instead the rates proposed by Staff should be adopted as proper and reasonable.

Time Warner argues that its 1240 filing is fair and accurate and that the charge attributable to NY1 programming has been fully supported and should be included in setting the rate for Time Warner's basic service tier. According to Time Warner, FCC rules state that if a prevailing company price has not been established for affiliate programming, the only other alternative for evaluating affiliate transactions involving programming is net book cost. Time Warner contends that it should not be required to provide the level of support data requested by Staff and RPA for a single program network such as NY1. Finally, Time Warner claims that the burden of proof should be placed upon the RPA and Staff to prove that the filing is incorrect rather than upon Time Warner to prove that the filing is just and reasonable.

The RPA argues that Time Warner failed to provide the data necessary to support its claim to increase rates for the basic service tier. Specifically, Time Warner failed to substantiate that its claimed expenses for NY1 were appropriate to pass on to ratepayers. The general ledger supplied by Time Warner is insufficient, by itself, to allow the ALJ and the Board to determine whether the programming cost associated with NY1 is appropriate to pass through to ratepayers. Accordingly, RPA concludes that an appropriate cost basis has not been provided, and therefore the Board and the ALJ have no choice but to recommend disallowance of any cost pass-through to subscribers.

Staff contends that Time Warner failed to provide sufficient support for the cost per subscriber, per month, during the true-up period and projected period for programming costs it claimed were charged by its local news programming affiliate NY1. Since Time Warner failed to provide evidence to reasonably support a determinable level of NY1's programming costs, a calculation on the basis of actual net book costs could not be used and an alternative approach was offered. Staff maintains that the FCC rules in 47 C.F.R. § 76.924 identify three specific methods for valuing transactions between cable companies and their affiliates: prevailing

company pricing, estimated fair market value, and net book cost. Under these rules, in the absence of a prevailing company price, the cost of programming should be the lower of the provider's net book cost or the programming's estimated fair market value. At hearings, Time Warner indicated its parent charges a third party non-affiliate \$0.37 per subscriber per month for NY1 News while claiming a charge to its Bergen system of a weighted average of \$0.51 in the true-up period and \$0.63 in the projected period. According to Staff, such information represents a fair estimation of market value for a local news channel such that the \$0.37 is the appropriate cost to be imputed to NY1.

The Board agrees with the determination of ALJ Gural that Time Warner failed to meet its burden of proof. Time Warner was asked to provide all supporting documentation, studies, analysis, reports, or other work papers showing that the programming cost charged to Time Warner for NY1 is cost-based. In response, Time Warner, provided only a half-page, single step summary of costs. Time Warner never provided a written copy of any programming contract for the NY1 channel. The Board finds these submissions to be insufficient to allow the Board to determine the reasonableness of the proposed rates. The Board further agrees with ALJ Gural's finding that Time Warner's provision of ledger entries just two days before hearings was not sufficient to satisfy cost of service scrutiny for its NY1 programming affiliate under FCC rules. The general ledger presented contained only controlling or summary rather than detailed accounts. ALJ Gural recognized that the submission of this type of document to support a cost of service claim by a cable television system is contrary to FCC rules, which clearly expect cable operators to provide detailed disclosure of affiliate transactions. See In the Matter of Implementation of Sections of the Cable Television Consumer Protection and Competition Act of 1992: Rate Regulation and Adoption of A Uniform Accounting System for Provision of Regulated Cable Service, 9 F.C.C.R. 4527, ¶ 271. Likewise, the Board also agrees with the ALJ's findings that the proposed rates calculated by the Staff are just and reasonable, that RPA's proposed rate of \$0.00 is inappropriate, and that Time Warner did not successfully justify its proposed rates. Finally, the Board also agrees with the analysis of ALJ Gural noting that, under FCC rules, in the absence of a prevailing company price, the cost of programming should be the lower of the provider's net book cost or the programming's estimated fair market value, and that, in the present case, the proper value is \$0.37.

Accordingly, after review, the Board HEREBY ADOPTS the recommendation of ALJ Gural and HEREBY FINDS that Time Warner is in default under 47 C.F.R. § 76.937 by failing to demonstrate the reasonableness of its rate for NY1 on the submitted FCC Form 1240. The Board FURTHER FINDS that, based upon this default, the Board may, consistent with 47 C.F.R. § 76.937(d), enter an Order finding the cable operator's rates unreasonable and mandating appropriate relief. Finally, the Board FURTHER FINDS that the rates charged by Time Warner for the NY1 channel are unreasonable and not supported by the record. Thus, the Board HEREBY ORDERS that the FCC Form 1240 submitted by Time Warner is rejected to the extent that NY1 is listed at any rate other than \$0.37 per subscriber, and a per subscriber rate of \$0.37 shall be substituted.

#### FCC FORM 1205

ALJ Gural found that Time Warner did not meet its burden of proof, required under 47 C.F.R. § 76.937, in support of its FCC Form 1205 filing. Because of this failure, the ALJ found that Time Warner's Maximum Permitted Rates (MPRs) should be those provided by Staff in its Reply Brief, Attachment-B (SRB-2), annexed to the Initial Decision. ALJ Gural specifically noted that those categories in the Form 1205 filing which had not been previously "carved out" of the original Form 1200 or subsequent Form 1205 should be excluded to ensure that Time Warner did not double recover on the costs. ALJ Gural noted, however, that this determination

did not require the entire Form 1205 to be excluded, and that those elements that were not rejected could be used as the “best information” for a revised filing. ALJ Gural additionally found the proposed rates calculated and proposed by Staff (SRB-2) to be just and reasonable. Finally, ALJ Gural found that, while Time Warner has the discretion to carry WLNY in its Basic Service Tier (BST) in a digitally compressed signal format, because this carriage would require a high-end converter box to accommodate the digital signal in an otherwise analog basic tier, Time Warner should be required to supply the converters to BST-only customers at either no charge or at the analog equipment rate.

Time Warner believes that its FCC Form 1205 filing is fair and accurate and that it provided additional back-up information and discovery responses sufficient to satisfy its burden of proof under 47 C.F.R. § 76.937. Time Warner stated that its FCC Form 1205 filing is a national aggregation, allowed and approved under the appropriate FCC regulations. Because of this aggregation, Time Warner indicates it should not be required to provide any additional level of back-up support data as requested by RPA or Staff. Time Warner states that the burden of proof should be placed on the RPA and Staff to prove that the FCC Form 1205 filings are incorrect, and that it is inappropriate to go back in time to the FCC Form 1200 filings that were filed by its predecessors and originally used to create an unbundling of the basic programming and installation and equipment benchmark rate. Time Warner claims that it cannot locate the FCC Form 1200 work papers and therefore the review should be done using only the best available information. As to the digital converter issue, Time Warner claims that cable operators are not required to offer equipment specific to the BST tier, and that because it does not supply analog only converters in its Bergen system, the charge would be the same even if WLNY was broadcast in an analog format. Finally, Time Warner notes that the Board does not have jurisdiction over the carriage or non-carriage of WLNY, the placement of WLNY, or its method of delivery.

The RPA contends that Time Warner fails to provide the necessary support for its proposed rate increases. RPA believes that not all the costs in the FCC Form 1205 should be rejected, but that those costs not previously included with the original FCC Form 1200 and subsequent FCC Form 1205 must be excluded, to avoid a double recovery on the costs. The RPA witness identified the expense items in the current FCC Form 1205 that were not separated out for inclusion under FCC Form 1205 filings when the original FCC Form 1200 was filed. Removal of these items, according to the RPA, will result in an acceptable MPR. Further, the RPA claims that, when a cable operator selects to provide a digital broadcast channel on its BST, it follows that the cable operator must provide a digital converter at either no charge or at an appropriate basic analog rate. Despite listing two converter rates – a digital converter at \$4.40 and an analog converter at \$0.59 – Time Warner does not offer the lower converter rate in the Bergen system. RPA asserts, however, that under the FCC’s ruling in its Aggregation Order, I/M/O Implementation of Section 301(j) of the Telecommunications Act of 1996, 11 F.C.C. Rcd. 6778, ¶ 6 (1996), Time Warner is obligated to charge Bergen system BST customers the lowest equipment price even when BST only subscribers are provided with more expensive equipment normally used by non-BST-only subscribers.

Staff argues that Time Warner improperly allocated certain expenses and costs used in computing the equipment rates and installation charges that resulted in overcharges to subscribers. Specifically, Staff’s arguments are that: a) Time Warner has failed to demonstrate that the capital costs and operating expenses it seeks to recover in its FCC Form 1205 filing were appropriately unbundled pursuant to the FCC Forms 1200/1205 process and therefore must be removed from Time Warner’s filing in the calculation of the equipment and installation charges for New Jersey customers, b) both FCC rules and case precedent clearly support Staff’s position that costs for installation and maintenance in “Schedule A” and operating

expenses in "Schedule B" that were not unbundled in the system's 1200/1205 filing must be removed, absent appropriate adjustments to Time Warner's base rate, and c) Time Warner's failure to propose a converter rate for "basic-only" customers is contrary to FCC regulations and Congress' intent to prevent subsidization by "basic-only" subscribers of the costs of more advanced equipment required by "non-basic" subscribers.

### Burden of Proof

The Board agrees with the finding of ALJ Gural as to the failure of Time Warner to satisfy the burden of proof. Time Warner failed to meet its burden, as required under 47 C.F.R. § 76.937, and, despite being given an opportunity to cure defects in its filings, did not provide sufficient information to allow the Board to determine the reasonableness of its rates. The Board agrees with ALJ Gural's determination that Time Warner failed to meet the reasonable discovery deadlines set out in the Prehearing Order, failed to provide full and complete responses to interrogatories, failed to provide a witness with full knowledge of the rate filing, and failed to comply with the FCC requirements for a rate proceeding. 47 U.S.C. § 543; 47 C.F.R. §§ 76.922, 76.923 and 76.937.

In order for the Board to approve of proposed rate increases, the burden of proof to show the reasonableness of the rates rests squarely upon the cable operator. 47 C.F.R. § 76.937. In order to facilitate this process, the Board may require the filing of supplemental information, may set reasonable deadlines and may impose sanctions, as required. In a contested case, such as this, the ALJ may do the same. N.J.A.C. 1:1-13.2. Here, ALJ Gural issued a Prehearing Order on January 27, 2003, setting out the schedule for completion of discovery, and specifically noting the need to pre-file testimony. Time Warner failed to conform to this schedule on a number of occasions, and likewise provided incomplete discovery throughout the proceedings. Time Warner, in response to a motion to compel outstanding discovery, provided some additional information, although never supplied all the discovery requested, and submitted some as late as May 5 and 6, or just days before the May 8 and 9 hearing dates.

During the hearings, Time Warner placed Terrence Rafferty, Vice President for Finance with Time Warner, on the stand to provide information about the preparation and data involved in the national FCC Form 1205 submitted. During his testimony, Rafferty indicated that he was only involved in the preparation of the FCC Form 1205 to the extent that he prepared the Bergen version. Rafferty indicated that he could only attest to 13% of the data used to fill out the National FCC Form 1205 submitted in this matter. Following this testimony, Time Warner offered to provide the testimony of James Jeffcoat, a Vice President of Strategic Procurement and the individual responsible for the preparation of the National FCC Form 1205. Staff and the RPA objected, as Jeffcoat had not been disclosed as a witness and had failed to pre-file testimony as required under the Prehearing Order. Accordingly, ALJ Gural denied Time Warner's request to place Jeffcoat on the stand. Then, in its brief following the hearing, Time Warner included a certification from Jeffcoat. ALJ Gural rejected this as well. The Board agrees with this determination on the part of ALJ Gural, finding that, under N.J.A.C. 1:1-14.14(a), the exclusion of the certification was an appropriate response on the part of the ALJ to Time Warner's failure to disclose or pre-file testimony from Jeffcoat.

When a cable operator has failed to satisfy its burden of proof and failed to meet reasonable deadlines or otherwise provide information in good faith, the FCC remedy is clear. Pursuant to 47 C.F.R. § 76.937, the Local Franchising Authority, in this case the Board, may find the operator in default and may, using the best information available, enter an order finding that the cable operator's rates are unreasonable and order appropriate relief; such as prospective

rate reductions, proscribing a reasonable rate and ordering refunds. 47 C.F.R. §§ 76.940, 941 and 942.

Accordingly, after review, the Board HEREBY ADOPTS the recommendation of ALJ Gural and HEREBY FINDS that based upon the failure to conform to the Prehearing Order, the testimony and certification of Jeffcoat was properly excluded, and therefore Time Warner failed to satisfy its burden of proof in showing that the rates proposed were reasonable. The Board FURTHER FINDS that Time Warner is in default and that, under 47 C.F.R. § 76.937, the Board may, subject to 47 C.F.R. § 76.937(d), enter an Order finding the cable operator's rates unreasonable and mandating appropriate relief. Based upon the foregoing, the Board HEREBY ORDERS that, Time Warner shall only charge customers rates that conform with those proposed in SRB-2 and approved in the Initial Decision of ALJ Gural, as discussed further below.

#### FCC Form 1200 Excluded Costs

The Board agrees with the finding of ALJ Gural that Time Warner must remove those identified costs that had not been excluded under the original FCC Form 1200 filing and which, if included, would have resulted in a double recovery of expenses on the part of Time Warner. Time Warner's attempt to seek to recover costs and expenses in its FCC Form 1205, Schedules A and B, which had not been identified in the Bergen New Jersey system's Forms 1200/1205 proceedings, is inappropriate. The Board must note, however, that ALJ Gural's finding that Time Warner should exclude the identified categories does not mean that the entire FCC Form 1205 should be excluded; the remainder of the Form is used to provide the "best information" possible upon which rates shall be based. Only those items that were not excluded under the FCC Form 1200 filing, and for which continued inclusion would constitute a double recovery, must be excluded.

The issue of cost recovery in the equipment basket of FCC Form 1205 filings after a cable system's initial unbundling is not a new issue, and has been addressed by the FCC both in its rules and as part of its decisions addressing appeals of local rate orders. The FCC has clearly ruled that any costs not unbundled or removed from Form 1200 during the initial process are, therefore, recovered in the basic service rate, because the initial unbundling process in the FCC Forms 1200/1205 created a direct linkage between the basic rates, equipment and installation charges. Due to this linkage, cable operators who find that an initial unbundling was inadequate, does not reflect current costs, or is otherwise flawed, must, according to the FCC, remove the costs not unbundled in the 1200/1205 process from its base rate calculation for its basic service tier and make appropriate going forward adjustments to that rate, in order to avoid a double recovery of those costs. I/M/O TCI Cablevision of St. Louis, Inc., 12 F.C.C. Rcd. 15,287, 15,289 (1997). This requirement is unaffected by time, or a change in the way a cable operator currently treats those costs. See I/M/O TCI Cablevision of Oregon, Inc. d/b/a TCI of Tualatin Inc., 1999 WL 958605, ¶ 5 (1999).

Accordingly, after review, the Board HEREBY ADOPTS the recommendation of ALJ Gural and HEREBY FINDS that Time Warner may not include in its FCC Form 1205 filing those identified categories which had not been excluded from the rate under the initial FCC Form 1200 unbundling process. Thus, the Board HEREBY ORDERS that Time Warner shall charge rates in conformity with those proposed in SRB-2 and approved in the Initial Decision of ALJ Gural, and limited to those categories and expenses previously unbundled through the FCC Form 1200 filing.

#### Digital Channel on BST

The Board agrees with the finding of ALJ Gural, with slight modification, that while Time Warner may carry WLNY on its BST in a digitally compressed format, Time Warner must nonetheless provide the necessary converter to receive WLNY at no charge or at the same rate as the analog equipment rate for the WLNY service.

FCC regulations provide that the costs of equipment used by basic-only subscribers may not be aggregated with the more advanced equipment used by non-basic-only subscribers. 47 C.F.R. § 76.923(c)(2)(B); I/M/O Implementation of Section 301(j) of the Telecommunications Act of 1996, 11 F.C.C. Rcd. 6778, ¶ 6 (1996). These rules also provide for an alternative method, whereby cable operators may base their basic-only subscriber cost allocation on the lowest and least expensive model of equipment offered, even if some basic-only subscribers actually have higher-level, more expensive equipment. In adopting this regulation, the FCC stated “[w]e conclude that Congress intended to ensure that basic-only subscribers not bear the costs of equipment used by subscribers taking services in addition to basic.” Id., at ¶ 23.

In this filing, Time Warner has frustrated Congress’ intent and the requirement of the FCC regulation that sought to prevent subsidization by basic-only subscribers of the costs of more advanced equipment by failing to provide a separate converter rate for basic-only subscribers. Time Warner has proposed a single rate of \$4.40 for all customer equipment to customers in the Bergen New Jersey system. Even though Time Warner indicates a lower converter rate of \$0.51 in its National Aggregate FCC Form 1205 filing, Time Warner claims that this equipment is not available to customers in the Bergen system, and therefore the price need not be offered.

The Board believes the FCC’s intent is clear, and while Time Warner has elected to aggregate its equipment costs on a national level, and appear to not offer a basic-only type converter in its Bergen systems, it must nevertheless charge Bergen customers on the basis that all basic-only subscribers use the lowest level and least expensive model of equipment it offers, no matter the equipment actually used. Accordingly, after review, the Board HEREBY ADOPTS the recommendation of ALJ Gural and HEREBY FINDS that Time Warner may charge no more than the basic converter rate listed in its National FCC Form 1205 for any equipment necessary for basic only subscribers to receive BST service. The Board FURTHER FINDS that Time Warner’s decision to neither supply the basic level converter in the Bergen system nor broadcast WLNY in an analog format does not relieve it of the responsibility to provide BST customers with the equipment necessary to receive BST service at the lowest equipment cost. The Board FURTHER FINDS that the rate to be charged for the converter needed to receive WLNY should be \$0.51 as identified in SRB-2. The Board believes that ALJ Gural’s acceptance of Staff’s MPRs in SRB-2 included his acceptance of the \$0.51 set forth as the cost for the converter necessary to receive the full complement of channels in the BST, including WLNY. Therefore the Board HEREBY ORDERS that Time Warner shall provide a digital converter to receive BST service with a cost based upon that proposed in SRB-2 and approved in the Initial Decision of ALJ Gural.

#### Additional Elements

To the extent not otherwise discussed, the Board HEREBY ADOPTS the recommendations of ALJ Gural, for substantially the reasons presented in the Initial Decision. To the extent that adoption of the Initial Decision as outlined above results in a refund liability for overcharges associated with Time Warner’s Form 1240 and 1205 rates, Time Warner is HEREBY ORDERED to provide a refund liability statement within 30 days of the date of this Order, and, following review and approval by Staff, Time Warner shall provide refunds to

subscribers within 60 days of the date of this Order. The refunds shall be listed as "BPU Refunds" on the subscribers' bills, and, pursuant to 47 C.F.R. § 76.942(e), shall include interest up to the date of distribution of the refund. Proof of refund shall be submitted to the Board within 10 days of its distribution.

DATED: August 19, 2003

BOARD OF PUBLIC UTILITIES  
BY:

(signed)

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JEANNE M. FOX  
PRESIDENT

(signed)

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FREDERICK F. BUTLER  
COMMISSIONER

(signed)

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CAROL J. MURPHY  
COMMISSIONER

(signed)

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CONNIE O. HUGHES  
COMMISSIONER

ATTEST:

(signed)

KRISTI IZZO  
SECRETARY



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